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A PLAN TO ENCOURAGE EQUITY INVESTMENT BY INDIVIDUAL CANADIANS

A Proposal by the Government of British Columbia to the First Ministers' Conference on the Economy

Honourable W. R. Bennett
Premier

Province of British Columbia

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The Canadian economy is currently characterized by a unique set of circumstances. Inflation and interest rates are both lower than they have been in several years and both may continue to decline over the short term. After several years of real decline, business fixed investment is expected to begin to grow again in response to the world economic recovery and as existing plants are modernized to incorporate new technologies. Finally, as the result of the extreme economic uncertainty that has been experienced in recent years, personal savings rates are at an historically high level.

Given these factors, a unique opportunity is available to Canadian governments to positively affect the structural transformation which is already underway in the Canadian economy. It is the view of the Government of British Columbia that economic recovery will be more lasting, and necessary structural adjustments will occur more quickly and more smoothly, if the recapitalization of Canadian industry can be financed by the large pools of domestic savings held by individual Canadians.

The channeling of these savings into equity investments to finance modernization, upgrading and expansion of the country's industrial structure would have a number of positive benefits. First, it would ensure that Canadian industry is able to undertake required new investment without having to incur long-term risks associated with a heavy burden of fixed debt. The experience of recent years, which saw many fundamentally viable companies struggling to cope with excessive debt, suggests the desirability of this course.

Second, the utilization of domestic savings to finance anticipated investment activity would minimize exchange and interest rate disruptions that might otherwise occur, and could help shield Canadian industry from international economic uncertainty. Third, and perhaps most important, the mobilization of the savings of individual Canadians to finance the economic and industrial transformation of the 1980s and 1990s would instill in individual Canadians a sense of direct participation in the economic future of the country.

The benefits resulting from increased equity ownership by individual Canadians in Canadian public companies would include: a greater willingness on the part of individuals to bear risk, a better general understanding of the function of profits in the economy, an increased awareness of the reality of business cycles and economic adjustments and an enhancement of the entrepreneurial spirit of individual Canadians.

The Government of British Columbia recognizes that income from equity investments already receives preferential treatment under the Canadian tax system. Further tax preferences for income received in the form of dividends or capital gains arising from equity investments are probably not appropriate. Rather, what is required is a new instrument to provide both a direct incentive for individuals to become equity participants in Canadian companies for the first time and a degree of downside risk protection for new investors. To this end, the Government of British Columbia pro-

poses that the consideration be given to the implementation at the national level of a Canada Equity Plan. The proposed plan would have the following characteristics:

- Individuals resident in Canada who purchase *newly issued* common shares of a Canadian public corporation traded on a Canadian stock exchange would be entitled to an income tax credit of 20 per cent of the price of the shares.
- The maximum Canada Equity Plan tax credit available to an individual taxpayer would be restricted on an annual basis and as a percentage of taxable income (e.g., to $2,000 per year not to exceed 20 per cent of taxable income).
- Canada Equity Plan tax credits would be recaptured by the tax system when plan shares are sold. The suggested credit recapture rate is 10 per cent of the selling price of plan shares with total credit repayments not to exceed the total value of all credits originally claimed by the investor. To encourage investors to hold shares for an extended period, a higher rate of credit recapture would apply for plan shares sold in the first year after purchase. Under these repayment provisions, credits would be fully recaptured in the case of plans that experienced significant capital gains but would only be partially recaptured in the case of plans that made modest gains or experienced losses.
- It is suggested the cost of the plan be shared by the federal government and the provinces on a two-thirds/one-third basis.
- The annual net direct cost of the program would depend on share price movements and the number of plan participants, but would probably not exceed $100–$200 million per year for all governments. This cost would be consistent with an infusion of $1–$2 billion of equity investment in the economy annually.

The program outlined here is simple and modest in cost, but has significant potential to inject new vigor into the Canadian economy. It is hoped that it will be given serious consideration by the First Ministers of Canada.

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